November 20, 2019

Maybank

FX Flash

RMB - Further Gains May be Elusive

China Prioritizes Growth

PBoC cut 1Y loan prime rate by 5 bps, in line with our expectations, to 4.15%. 5Y loan prime rate was also cut to 4.80% from 4.85%. This is the second time PBoC had lowered LPR since it introduced the new policy rate in Aug at 4.25%. There could be further rate cuts in the next few months and a shift towards greater support for the domestic economy could mean that China want to cushion its economy against further headwinds in case of another fall-out with the US. **We close our short USDCNH position at 7.03 and look for USDCNH to head towards 7.10 (our year end forecast).**

We had looked for China to cut after the soft macro performance and following the 5bps cut in the MLF (on 5 Nov) as well as 7-Day reverse repo rate (on 18 Nov). A cut today could ensure that the newly-introduced policy rate would be in line with these lending rates that central bank uses to provide financing for financial institutions.

Bear in mind that the three intents of the rate reform were

1) to have a more market-based rate,
2) lower real lending rates,
3) to improve the efficiency of interest rate transmission.

Lowering the new loan prime rate today reinforces easing bias, strengthens its link to medium-term lending facility rate (also cut from 3.30% to 3.25% on 5 Nov) as well as the 7-day reverse repo rate (also lowered from 2.55% to 2.50% on 18 Nov) and concomitantly improve the policy transmission.

The 5bps cut is also in line with the recent 3Q monetary policy report released last week. Within the report, PBoC promised the use of targeted RRR cuts to improve credit and assures that inflation is still under control in spite of uncertainties. The central bank also sees increasing downward pressure on the economy. In response, there would be more “counter cyclical adjustment”. New loans will be affected as they are priced based on the LPR when it was introduced in Aug.

USDCNH was bid this morning but upticks seem to be reined in by the USDCNY fix (7.0118) this morning, which came in to be lower than our estimate at 7.0157. The recent weeks of RMB stabilization and low currency volatility environment has given the central bank room to ease rates. Lowering policy rates in a weak RMB and strong USD environment could risk increasing the depreciation pressure on the currency.

Analysts

Saktiandi Supaat
(65) 6320 1379
saktiandi@maybank.com.sg

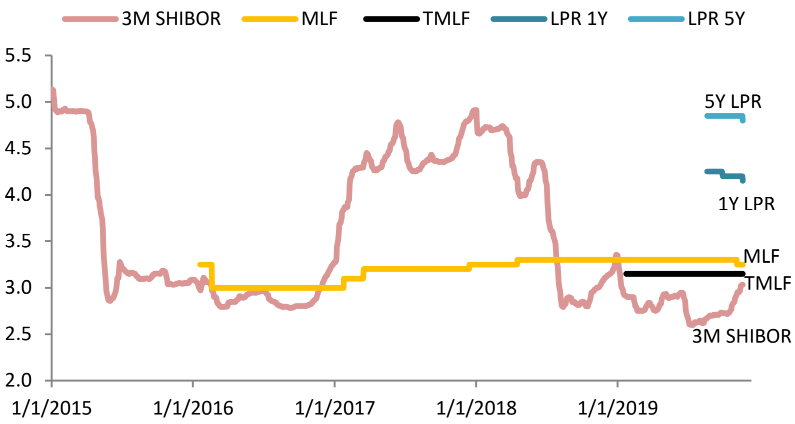
Fiona Lim
(65) 6320 1374
fionalim@maybank.com.sg

Tan Yanxi
(65) 6320 1378
tanyx@maybank.com.sg

Christopher Wong
(65) 6320 1347
wongkl@maybank.com.sg

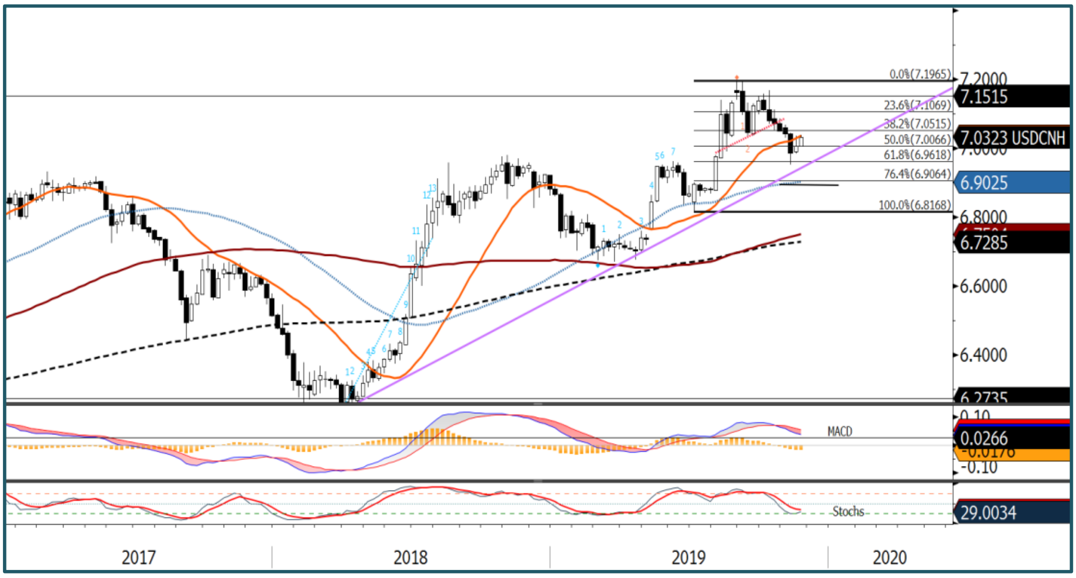
SEE PAGE 4 FOR IMPORTANT DISCLOSURES

PBoC Lowers 1Y LPR For the Second Time



Source: *Bloomberg, Maybank FX Research & Strategy*

<u>USDCNH (Weekly) – Oversold</u>



Source: Bloomberg, Maybank FX Research & Strategy

We take the opportunity to <u>close our short USDCNH position at 7.03 (with a profit 1.1%)</u> as we see potential for this pair to head higher towards 7.10 as stochastics start to rise from oversold condition on the weekly chart.

<u>Hong Kong Bill Could Be a Hurdle</u>

We are also wary of US-China relations souring further after the US Senate passed the bill to support the Hong Kong protestors and warning China against a violent suppression of the demonstrations. The bills that were passed by the Senate were a tad different from those passed by the House of Representatives and these two versions will need to be reconciled into 1 unified bill before being returned to each chamber for final approvals before it reaches Trump. China had just responded with threats of retaliation along with reiterations for the US to "stop interfering in Hong Kong affairs". While Trump has shown little support for the bill, it would be difficult for him to veto a bill that has bipartisan support.

FCC Vote, US Treasury FX Report

There are a few other events that we monitor - 1) the US Federal Communications Commission vote on 22 Nov to name Huawei and ZTE as "threats to national security" which would block local carrier customers from using government funding to purchase equipment and services from the two companies. That could risk US-China relation even though Huawei may no longer be a priority for Beijing in the phase 1 of trade deal. We also watch out for 2) the FX report (typically released twice a year) by the US Treasury and investors could be disappointed if the designation of "currency manipulator" for China remains.

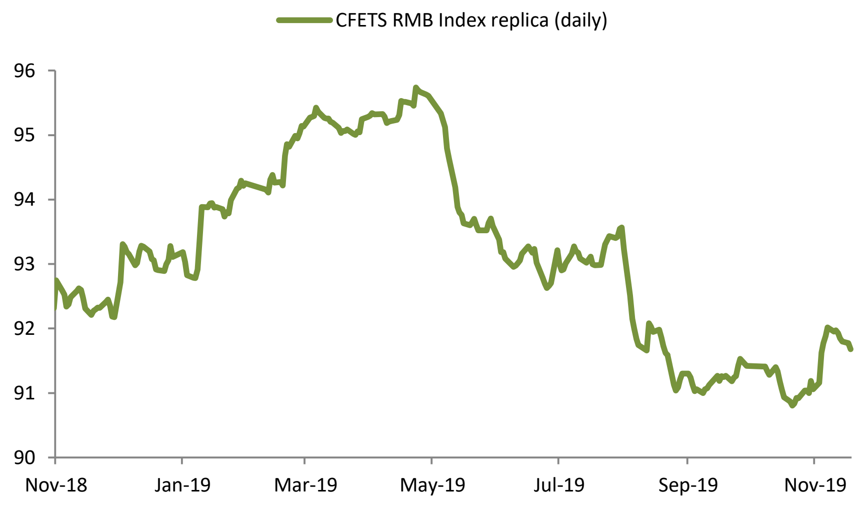
In addition, a few days ago, a CNBC Beijing Bureau Chief Eunice Yoon cited sources commenting about China's apprehension over the upcoming trade deal after Trump said he has not agreed to a rollback of tariffs – an agreement in principle between top officials on both sides recently. In a tweet, she reported, "*strategy now to talk but wait due to impeachment, US election. Also, prioritize China economic support*".

Eyes are on a deal before 15th Dec

That priority on "economic support" has certainly come true with the lowering of the LPR, small as the magnitude of the cut may be. There could be further rate cuts in the next few months and a shift towards the domestic economy could mean that China want to cushion its economy against further headwinds in case of another fall-out with the US on trade-talks.

At this point, we like to take into consideration an increasingly possible scenario that phase 1 of the trade deal may not come so soon. Within the next few weeks, the Hong Kong bill would need to be ironed out by the two Houses of Congress in the US (that could elicit retaliation as threatened by China), impeachment proceedings against Trump may gain traction that could cast doubt on China's resolve to reach a deal. Since the cancellation of the Chile APEC summit, the venue and date of the deal have not been decided. That would mean that China is at risk of being slapped with another tranche of 15% tariff on an estimated $156bn of goods on 15th Dec, as threatened by Trump in his remarks at the Economic Club of New York last week. In the meantime, Trump promised another "cash payout" to local farmers ahead of Thanksgiving (part of the package announced in May). The next tranche would be paid out in Jan 2020 if the trade war continues.

CNY TWI has been Weakening Since Early Nov



Note: The above index is based on daily CNY fixes

Source: Bloomberg, Maybank FX Research & Strategy

In the near-term, USDCNH (last seen at 7.0334) seems to be gaining on bullish momentum and a break of the 7.0515 would open the way towards 7.0730 (50-dma) before the next at 7.1070 (23.6% Fibonacci retracement of the Jun-Aug rally). Support at 7.0066 before 6.9620. As we have noted in the earlier part of this report, the weekly chart is also showing bullish bias. The CNY daily reference rate has been fixed on a weakening bias (against its trading partners) since early Nov.

DISCLAIMER

Published by:

Maybank

Malayan Banking Berhad
(Incorporated in Malaysia)

Saktiandi Supaat	Christopher Wong	Fiona Lim	Yanxi Tan
Head, FX Research	Senior FX Strategist	Senior FX Strategist	FX Strategist
saktiandi@maybank.com.sg	wongkl@maybank.com.sg	Fionalim@maybank.com.sg	tanyx@maybank.com.sg
(+65) 63201379	(+65) 63201347	(+65) 63201374	(+65) 63201378